



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	06/26/03	Bill No:	AB 1666
Tax:	Cigarette and Tobacco Products	Author:	Cogdill
Board Position:		Related Bills:	

BILL SUMMARY

Among other things, this bill would:

- Allow a distributor to elect either a monthly or twice-monthly payment basis for amounts owing for stamps and meter register settings purchased on a deferred basis;
- Reduce the amount of security required to be posted by a distributor that defers payments for stamps and meter register settings and elects a twice-monthly payment basis, from 70 percent to 50 percent, of the amount of stamps and meter register settings for which payment is deferred;
- Allow a distributor of tobacco products to elect either a monthly or twice-monthly basis to file a return and remit payment of the amount of tax due respecting his or her distributions of tobacco products and their wholesale cost during the preceding month.

Summary of Amendments

The amendments to this bill since the previous analysis require that the reduced security amount only apply to distributors that elect to make deferred payments on a twice-monthly basis, replace Assembly Member Campbell with Assembly Member Cogdill as the bill's author, and add that the act is an urgency statute.

ANALYSIS

Current Law

Under current Cigarette and Tobacco Products Tax Law, an excise tax of 43 1/2 mills per cigarette (87 cents per package of 20) is imposed on each cigarette distributed. The cigarette tax imposed with respect to the distribution of cigarettes is paid by distributors through the use of stamps or meter impressions. An appropriate stamp or meter impression is required to be affixed to, or made on, each package of cigarettes prior to distribution of the cigarettes, except as otherwise provided.

Current law also imposes a surcharge on tobacco products at a rate to be annually determined by the Board. The tobacco products tax rate is equivalent to the combined rate of tax on cigarettes. Currently, the surcharge rate for fiscal year 2002-03 is 48.89 percent.

Every applicant for a license as a distributor is required to file with the Board security in the amount and form as the Board prescribes. The minimum security that is required of any distributor is one thousand dollars (\$1,000). However, distributors desiring to defer payment for stamps and meter impressions are required to furnish a security equal to not less than 70 percent of the amount and not more than twice the amount of the

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purchase of stamps and meter register settings for which payment may be deferred. Amounts owing for stamps and meter register settings purchased on a deferred payment basis in any calendar month are due and payable to the Board on or before the 25th day of the following calendar month.

Each distributor of tobacco products is required to file a return on or before the 25th day of each month respecting his or her distributions of tobacco products and their wholesale cost during the preceding month and such other information as the Board may require. Each distributor of tobacco products is also required to remit the amount of tobacco products tax due to the Board on or before the 25th day of the calendar month following the close of the monthly period for which it relates.

Proposed Law

This bill would amend Section 30142 of the Cigarette and Tobacco Products Tax Law to reduce the security required to be provided by a licensed distributor desiring to defer payments for stamps or meter register settings and elect to make deferred payments on a twice-monthly basis. Specifically, the amount of the security required would be equal to not less than 50 percent of the amount and no more than twice the amount, as fixed by the Board, of the distributor's purchases of stamps and meter register settings for which payment may be deferred.

This bill would amend Section 30168 to allow a distributor to elect a payment basis for amounts owing for stamps and meter register settings purchased on a deferred basis. A distributor would elect to make the payment on either a monthly basis or a twice-monthly basis. If a distributor elects a monthly basis, payment would be required to be remitted on or before the 25th day of the month following the month in which the stamps and meter register settings were purchased. However, if a distributor elects a twice-monthly payment basis, the payment would be due as follows:

- The first monthly remittance would be made on or before the 5th day of the month for those purchases of stamps and meter register settings that were made between the first day and the 15th day of the preceding month.
- The second monthly remittance would be made on or before the 25th day of the month for those purchases of stamps and meter register settings that were made between the 16th day and the last day of the preceding month.

This bill would also amend Section 30181 to allow a distributor of tobacco products to elect to file a return and make payment of the tax due on either a monthly or a twice-monthly basis. In addition, Section 30182 would be amended to allow a distributor of tobacco products to elect a monthly or twice-monthly filing basis for returns respecting his or her distributions of tobacco products and their wholesale cost during the preceding month and any other information as the Board may require. If a distributor elects a monthly basis, the distributor would be required to file a return and make payment of the tax on or before the 25th day of the month following the month during which the tobacco products were distributed. If a distributor elects a twice-monthly basis, the distributor would be required to file two returns and make two remittances during the month following the month during which the tobacco products were distributed as follows:

- The first monthly return would be required to be filed, together with the first remittance of tax, on or before the 5th day of the month for those distributions of tobacco products that occurred between the first day and the 15th day of the preceding month.

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- The second monthly return would be required to be filed, together with the second remittance of tax, on or before the 25th day of the month for those distributions of tobacco products that occurred between the 16th day and last day of the preceding month.

This bill would become effective immediately as an urgency statute.

In General

Every applicant for a license as a distributor is required to file with the Board a security in the amount and form as the Board prescribes. The minimum security that is required of any distributor is one thousand dollars (\$1,000). However, every distributor desiring to purchase tax stamps or meter register settings on the deferred payment basis would request the Board to set the maximum amount of such purchases the distributor may have unpaid at any time and the amount of the required bond. The maximum amount of stamps and meter register setting purchases for which the distributor may defer payment can not exceed one and one-half times the distributor's average monthly tax liability based on the distributor's previous six months' experience. Or in the case of a distributor not previously authorized to make deferred payment purchases or a distributor the character of whose business has changed substantially, the maximum amount will be set at one and one-half times the estimated average monthly tax liability as determined by the Board. When a distributor is authorized to purchase stamps or meter register settings on the deferred payment basis, the bond will be fixed in an amount equal to 70 percent of the amount of deferred payment purchases which the distributor may have unpaid at any time.

Once the required security is received, the Board provides written authorization for the amount of deferred payment purchases the distributor may have to the Bank of America branch where tax stamp and meter register settings purchases are to be made. The Board currently contracts with Bank of America to sell cigarette tax stamps to licensed distributors and to remit the tax collected to the Board.

Payment for all deferred payment purchases of tax indicia made during each calendar month must be made at the Bank of America branch office where the purchases were made, and must be made by the 25th day of the calendar month following the month in which the purchases were made. Remittance for such purchases are made payable to "State Board of Equalization." The privilege of making deferred payment purchases will be suspended if there is a delinquent balance owing.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the California Distributors Association and is intended to address the difficulty distributors experience trying to obtain bonds for deferred purchases of tax stamps. According to the author, two issues have had a distinct impact on this insurance. First, insurance companies have been forced to raise their rates and reduce policies since September 11, 2001. An average bond, if available, has risen from under 4 percent to over 6.5 percent of its value. Second, recent large judgments against manufacturers (not distributors) have had a chilling effect on bonding. Although most judgments have been lowered or dismissed all together, bond companies are still concerned. According to the sponsors, if bonds are not available, the cash requirements of all distributors would be impossible to meet.

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2. **Key amendments.** The **June 26, 2003**, amendments require that the reduced security amount only apply to distributors that elect to make deferred payments on a twice-monthly basis, replace Assembly Member Campbell with Assembly Member Cogdill as the bill's author, and add that the act is an urgency statute.

The **April 22, 2003**, amendments address a technical concern raised in the Board's analysis. These amendments align the due date for filing a return for the distribution of tobacco products with the due date for remitting payment of the tobacco product taxes.

3. **Suggested amendments.** Board staff is willing to work with the author's office in drafting appropriate amendments to address the following concerns:

- This bill would require a distributor to elect a payment basis for deferred purchases of tax stamps. They would have the option to elect either a monthly or a twice-monthly payment basis. However, this bill does not provide how often a distributor may change their elected payment basis. For example, could a distributor change their payment basis election each month? It is suggested a distributor's payment basis election be maintained for a specified period, such as one year.
- This bill does not specify a security requirement for a distributor that desires to defer payments for stamps or meter register settings and elects to make those deferred payments on a monthly basis. It is therefore recommended that Section 30142 be amended to require a security equal to not less than 70 percent of the amount and no more than twice the amount, as described in existing law, for a distributor that elects to make deferred payments on a monthly basis.
- Current law Section 30182(a) requires, on or before the 25th day of each month, every distributor to file a report respecting his or her distributions of cigarettes and purchases of stamps and meter register units during the preceding month. As such, distributors electing to make payment twice-monthly for amounts owing for stamps and meter register settings purchased on the deferred-payment basis would only be required to file a report once a month, but would make deferred payments twice-monthly. It is therefore recommended that Section 30182(a) be amended to require distributors that elect to make deferred payments on a twice-monthly basis to file two reports during the month. It is further recommended that the due date for each report be consistent with the proposed due date for deferred payments made on a twice-monthly basis.

4. **How would this bill affect the Board's contract with Bank of America?** The Board contracts with Bank of America to sell cigarette tax stamps to licensed distributors, to collect the cigarette tax, and to remit the tax collected to the Board. The Board's current contract with Bank of America is for the three-year period commencing July 1, 2001 and ending June 30, 2004. Accordingly, the Board would have to renegotiate its contract with Bank of America to accept payment for deferred purchases of tax stamps on both a monthly and a twice-monthly basis for the period of January 1, 2004 (the effective date of this measure) to June 30, 2004.

5. **Distributors purchasing tax stamps on a deferred basis.** Currently, 52 of the 242 distributors licensed with the Board purchase cigarette tax stamps on a deferred basis. The combined credit limit of these 52 distributors is approximately \$279 million, with a corresponding security of \$195 million (\$279 million x 70% = \$195 million). The Board is authorized to suspend a distributor's privilege to purchase tax

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stamps on the deferred basis if a distributor fails to promptly pay for stamps when payment is due. And if collection of these amounts remain unpaid, the Board could pursue the distributor's security.

There has been only one instance in the last ten years where the Board had to make a claim against a distributor's surety bond for non-payment of stamps and meter register settings purchased on a deferred payment basis. However, it is important to point out that very recently, a situation has arisen in which an outstanding deferred-payment balance was not paid by the due date. As of the date of this analysis, that balance is still outstanding.

6. **This bill should contain a specific appropriation to the Board.** This bill would allow a distributor to elect either a monthly or twice-monthly payment basis for the payment of amounts owing for stamps and meter register settings purchased on a deferred basis. In addition, this bill would allow a distributor of tobacco products to elect either a monthly or twice-monthly basis to file a return and remit payment of the amount of tax due respecting his or her distributions of tobacco products. If enacted, the provisions of this bill would require that implementation begin during the 2003-04 fiscal year. In order to begin to develop the fee payer base, reporting forms, and hire appropriate staff, an adequate appropriation would be required to cover the Board's administrative start-up costs that would not already be identified in the Board's 2003-04 budget.

COST ESTIMATE

The Board would incur costs related to this measure for notifying licensed distributors, developing returns, revising forms and publications, programming computers, and revising the Bank of America contract. A detailed cost estimate is pending.

REVENUE ESTIMATE

Enactment of this measure would have no impact on cigarette tax revenues. However, this measure would allow distributors the ability to elect a twice-monthly payment basis for deferred purchases of stamps and meter register settings. This could result in the Board depositing payments, as specified, approximately 20 days earlier for purchases of stamps and meter register settings that were made in the first 15 days of the previous month. As such, there is a potential for increased interest to the state on those deposited payments.

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